(31)

IN THE

Supreme Court of the United States

OCTOBER TERM—1943

No. 792

EDWARD D. LOUGHMAN, as Receiver of The Pelham National Bank, Pelham, New York,

Plaintiff,

against

TOWN OF PELHAM, Westchester County, New York,

Petitioner and Third-Party Plaintiff,

against

THE EMPLOYERS' LIABILITY ASSURANCE CORPORATION, LTD.,

Respondent and Third-Party Defendant.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

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March 14, 1944

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TO THE HONORABLE THE CHIEF JUSTICE AND THE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

The petitioner Town of Pelham respectfully prays that a writ of certiorari issue to review the Order of the United States Circuit Court of Appeals for the Second Circuit entered December 16, 1943 (R. 763). This affirmed the judgment of the United States District Court for the Southern District of New York entered March 1, 1943 (R.

NOTE: All references to the record before the Court below are in *folio* numbers. Because of the unavailability, at the time of completing this petition and brief, of folio numbers on the added pages containing the Opinions below and the further proceedings, references to those matters are necessarily in *page* numbers in that part of the record and have been written in.

13), which dismissed the third-party complaint of the Town of Pelham against The Employers' Liability Assurance Corporation, Ltd. The Receiver is not involved in the present litigation.

The majority and dissenting Opinions below are at R. P.54, and are reported in 139 Fed. (2nd) 989. The Opinion of the District Court is at R. 121.

A. Summary Statement of the Matters Involved

Principal facts giving rise to present questions are in the statement (R. P.52) preceding the Opinions below.

The action is upon the official bond of one Joseph H. McCormick as Supervisor of the Town of Pelham, in Westchester County, New York State. Town funds received by the Supervisor were admittedly lost.

At the time the Supervisor took office, the Town Law of New York required, as it had for many years (L. 1909, Ch. 63, Sec. 100), that the Supervisor give an official undertaking, with sufficient surety, that he would "well and faithfully discharge his official duties" and would "well and truly keep, pay over and account for all moneys and property" belonging to the Town and "coming into his hands as such Supervisor". The defendant Surety Company executed McCormick's undertaking as surety (R. 34, 40, 73, 75). The condition was that McCormick

> "shall pay over and account for all funds coming into his hands from January 1st, 1932 to December 31st, 1932, by virtue of his said office of Supervisor and shall well and faithfully perform all the duties of his said office"

only in which event McCormick and the Surety Company were to be released from liability to the Town for its funds (R. 34). The bond first given was extended, and covered the period within which Town funds were lost (R. 40).

The settled law and public policy of the State of New York, it will hardly be disputed and will be shown in our brief, had long been and then were that the Supervisor as the Town's chief fiscal officer was absolutely liable for Town funds, in the absence of clear and specific legislative provision relieving him from such liability upon his compliance with a statutory method of protecting the Town against loss of its funds.

At the time McCormick took office as Supervisor, the Legislature had not, we submit, relieved him from liability, but had provided a method by which he and his surety could protect and reimburse themselves in the event of the loss of Town funds. The Town Law at that time provided, as it had for many years (L. 1909, Ch. 63, § 101), that the Supervisor of a Town might, at the Town's expense,

> "purchase a surety bond of some solvent surety company, authorized to do business in the State of New York, securing to such Supervisor the safety of Town funds deposited by him in any bank or banking institution in this State, and indemnifying him against the loss thereof through the failure or insolvency of such bank or banking institution".

McCormick and his surety did not avail themselves of this statutory method for their protection.

Instead of doing what the Legislature had authorized him to do for his protection against his outright liability, McCormick, at the request of the Surety Company as a condition of its execution of his undertaking (R. 73), entered into an Escrow Agreement dated December 28, 1931, with The Pelham National Bank and the Mount Vernon Trust Company, whereby the Pelham Bank, as a condition of and to induce the Supervisor's depositing the Town's funds in that Bank, and for the particular purpose of indemnifying the Supervisor in the event of any loss of deposited funds, pledged in escrow with the Trust Company

$25,000 principal amount of Westchester County 4¼% Bonds due in 1968 (R. 79). This course of action by McCormick and the Surety Company gave rise, when the Pelham Bank became insolvent, to the Receiver's suit against the Town for the total proceeds of the escrow bonds and additional payments to the Town. In that litigation the Town prevailed as to retaining the proceeds of the escrow bonds (126 Fed. (2nd) 714).

The Town Board, on the motion of McCormick as its chief fiscal officer, had designated two banks and one trust company, all selected by him, "as depositaries for funds of the Town" (R. 72). He then chose to put and keep the Town funds in two of the three designated depositaries, and made no deposits at all in one of them (fol. 74). He chose to make the Pelham Bank his principal depositary, and kept Town funds there in a greater amount (fol. 64) than either the par value or the market value of the bonds (fol. 65) which he and the Surety Company had required to be deposited in escrow to protect them against their liability for the loss of Town funds. When the Pelham Bank closed its doors in 1933, never to reopen, McCormick had $27,862.92 of Town funds in that Bank (fol. 64).

This inadequacy of the escrow bonds fully to make good the amount of Town funds which McCormick had chosen to have in the Bank at the time it closed and failed gave rise to the present claim against the Surety Company, which has conceded that it is liable if the Supervisor was liable.

B. The Opinions Below

The majority in the Court below (R. [illegible]) recognized the New York rule of the outright liability of a Supervisor "for the net loss resulting from the Bank's failure", and would have enforced it, "were it not for § 149-c" of the Town Law. That provision was a part of a 1916

budgetary plan for certain Towns (L. 1916, Ch. 396), made applicable to the Town of Pelham in 1931 (L. 1931, Ch. 92).

This legislation contained no provision which, in terms or otherwise, even purported to relieve a Supervisor from liability for Town funds, nor did it repeal the provisions of Sections 100 and 101 of the Town Law above quoted. It even contained a "saving clause" negativing repeal and prohibiting any construction having the effect of repeal. The provisions, in pertinent part, were as follows:

> "§ 149-c. *Duties of Supervisor.* The Supervisor of any such Town shall demand, collect, receive and have the care and custody of and shall disburse all moneys belonging to or due the Town from every source, except as otherwise provided by law. All moneys of the Town received by the Supervisor shall be deposited by him in such bank, banks or trust companies as shall be designated by the Town Board for such purpose. * * * "
>
> "§ 149-e. *Saving clause.* Nothing contained in this article * * * shall be construed to repeal any statute of the State or lawful resolution of the board of supervisors of the County in which the Town is situated, or of the Town Board, or rule or regulation of the board of health of the Town, not inconsistent with the provisions of this article, and the same shall remain in full force and effect, when not inconsistent with the provisions of this article, to be construed and operated in harmony with its provisions."

With all deference, we submit that the dissenting opinion of Judge Swan more soundly construed and applied the local law designed for the protection of Towns from the loss of the funds raised by taxation. He adhered to the rule of absolute liability in the absence of express exemption based on an authorized method of full protection for the Town—the rule which the Court of Appeals enunciated in 1896 and has ever since applied without exception, and concerning which the Court of Appeals, in its latest decision on the

subject (1938), admonished that the rule was "too well established to be changed by the Courts" (*Bird* v. *McGoldrick*, 277 N. Y. 492, at page 499).

Judge Swan was of the opinion that the "principle of absolute liability has had so long a legislative recognition and has become so firmly entrenched in the case law of New York that I believe an express legislative mandate is required to get rid of it" (R. P. 62). He was unable to accept the view of the majority that the 1916 budgetary plan for Towns, made applicable to the Town of Pelham in 1931, warranted giving to Section 149-c, when taken in connection with Section 149-e, the effect of impliedly relieving the Supervisor of his liability for the loss of Town funds which he put and kept in one of the depositaries designated by the Town Board. He saw "no necessary inconsistency between requiring an official to deposit funds in a bank designated by other officers and requiring him to account if the deposited funds are lost", especially when the harshness of the rule of strict or absolute liability was expressly alleviated by a statute (Section 101) allowing the Town Supervisor to protect himself by obtaining a surety bond at the Town's expense (R. P. 62). Moreover, Judge Swan thought it "not without significance that when the new Town Law, effective in 1934, was enacted, the Legislature not only expressly relieved the Supervisor from absolute liability, but at the same time required him to procure a bond or take other security to protect the Town against loss resulting from a failure of a bank in which Town funds were on deposit" (R. P. 62). When the Legislature intended to relieve the Supervisor from his historic liability, this was stated expressly, and was coupled with a provision assuring full protection for the Town. Judge Swan declined to construe the 1934 legislation as merely confirming or codifying an exemption which had previously been made (in 1931) without words which even remotely implied an intent to exempt and were coupled with no provision assuring the protection of the Town in the

event of the loss of its funds through the failure of the depositary in which the Supervisor had seen fit to put and leave them.

C. Questions Presented

If this petition for review is granted, the primary question will be as to whether or not, under the statutes and decisional law of the State of New York at the time the Supervisor's undertaking was given and funds of the Town were lost, the Legislature of the State had abrogated the New York rule of a Supervisor's absolute liability to account for and pay over all monies coming into his hands as Supervisor, and had provided a substitute method which it intended should relieve the Supervisor but protect the Town; also, as to whether or not this Supervisor, the defendant Surety Company, and the Town, acted at that time on that basis and within the authority of such method, if any had been prescribed.

If this primary question is determined in the Town's favor, a further question in the litigation, not passed on by the Court below in view of its ruling on the primary question, will be as to whether or not the Surety Company is liable to the Town, as part of its surety obligation, also for the costs and expenses necessarily incurred by the Town in connection with this litigation to protect itself and its taxpayers against the loss of its funds.

D. Reasons Relied On for Allowance of the Writ

1. The Circuit Court of Appeals has decided an important question of local law in a way to be deemed in conflict with applicable local decisions, viz., those of the Court of Appeals of the State of New York. As Judge Swan's opinion below shows clearly, the rule of the public officer's strict and absolute liability to pay over and account for all public funds coming into his hands by virtue of his office, has long had legislative recognition and has become

firmly entrenched in the law of New York; and no authoritative New York case has ever recognized any exception to this rule of strict liability except that of loss due to an act of God or the public enemy. As to Town Supervisors in particular, having in mind the nature of local government outside of cities, it has long been the rule that Supervisors are absolutely liable for the funds they receive, unless and until the Legislature expressly exempts them upon their compliance with a prescribed method assuring the Town against loss. If the majority decision below were permitted to stand, it would set an objectionable and weakening precedent which is directly at variance with the public policy of the State and with numerous prior decisions by the New York Court of Appeals which have reiterated and enforced the liability of public officers receiving public funds.

2. The decision below has the effect of nullifying the express legislative policy and provisions of the New York Town Law which were designed to assure the safety, in any and all events, of the funds of local units of government such as Towns. Any doubt as to this effect of the decision below in this regard would be dispelled by examining the table of statutes in the Appendix hereto. Under the provisions of the New York Town Law in force when Supervisor McCormick took office and the loss took place, the Supervisor and the sureties on his official undertaking were absolutely liable to the Town for any loss of Town funds, even a loss resulting from bank failure; but the Supervisor, in recognition of this latter liability, was authorized to purchase, at the Town's expense, a surety bond "*securing to such Supervisor* the safety of Town funds deposited by him in any bank or banking institution in this State, and *indemnifying him* against the loss thereof". When the New York Town Law was subsequently amended (1934), the Supervisor and the sureties on his official undertaking were expressly relieved from liability for the loss of Town funds through bank failure; but the Super-

visor was required to purchase, at the Town's expense, a surety bond "*securing to the Town* the safety of Town funds deposited by him in or with any bank or trust company in this State, and *indemnifying the Town* against the loss thereof". At all times, the clear legislative intent and plan were that the Town funds should be secured from loss in any and all events. By its decision, the Circuit Court of Appeals has defeated the legislative plan and the basic law and policy, and has permitted the loss of the Town funds resulting from the failure of the Pelham Bank to fall upon the Town and its taxpayers, instead of upon the Town Supervisor and the surety on the official undertaking which the Surety Company executed and gave.

3. The decision of the majority in the Circuit Court of Appeals destroys vested contract rights and impairs the obligation of contract. Although professing otherwise, the majority gave essentially a *retroactive* effect to the later amendments to the New York Town Law, and did what the New York State Legislature did not do, and clearly did not intend to do, until some time after the rights of the Town against its Supervisor and his surety had become fixed. Actually, the majority Opinion imports into the explicit terms of the Supervisor's official undertaking a qualification which the Legislature, in amending the Town Law, made effective only upon the procurement by the Town Supervisor, at the Town's expense, of a surety bond *indemnifying the Town* against any loss of its funds when deposited in banks. No such bond was procured by the Supervisor in the instant case; on the contrary, McCormick, acting on his own initiative, for his own benefit, and at the request of the Surety Company, merely entered into a pledge agreement with the Pelham Bank, later held to be *ultra vires* and invalid. The only purpose of this pledge agreement was to indemnify the Supervisor against loss in the event of the failure or insolvency of the Pelham Bank; and the escrow agreement was obviously made with

reference to the express condition of Supervisor McCormick's official undertaking to "pay over and account for all funds coming into his hands" as Supervisor. McCormick, the Surety Company, and the Town, each knew and recognized the nature and extent of the obligation of McCormick's official undertaking, which contained no such qualification of obligation as the majority Opinion below now reads into the terms thereof; and the Surety Company should accordingly be held liable to the Town for the present loss pursuant to the express terms of its surety contract.

WHEREFORE, your petitioner respectfuly prays that a writ of certiorari be issued out of and under the seal of this Honorable Court, directed to the Circuit Court of Appeals for the Second Circuit, commanding that Court to certify and send to this Court for its review and determination, on a day certain to be therein named, a full and complete transcript of the record and of all proceedings in the case numbered on its Docket No. 18765, and entitled as above shown; and that the Order of that Court entered December 16, 1943, be reversed; and that your petitioner may have such other and further relief in the premises as to this Honorable Court may seem just and proper.

Dated: New York,
March 14, 1944

WILLIAM L. RANSOM

WILLIAM L. RANSOM
Counsel for Petitioner